against national ESPs -- the Commission's nonstructural safeguards are plainly not up to the task. The Commission should weigh this experience as it conducts its cost-benefit analysis.

1. **Cross-Subsidization.**

Southwestern Bell Audit. A joint federal-state audit of Southwestern Bell determined that Southwestern Bell's regulated operations cross-subsidized its unregulated operations by $93.7 million during the years 1989-1992.[99] The most troubling part of this audit was not the confirmation that the BOCs are capable of significant cross-subsidization of their unregulated activities, but rather the inability of regulators to even identify the problems after an extensive audit. Despite the best efforts of state and federal auditors, the accuracy of Southwestern Bell's cost allocations was impossible to determine.[100] The problem was neither the skill nor the resources of the auditors; Southwestern Bell kept its books in a manner that allocated charges without providing any supporting documentation.[101] If the BOCs are able to allocate costs without any basis, ITAA fails to understand how the Commission's accounting and auditing rules can effectively prevent cross-subsidization.

GTE Audit. The Commission conducted an audit of GTE for the years 1988 to 1990. The audit found significant cross-subsidization of GTE's unregulated activities.[102] Although the audit determined that cross-subsidization had occurred in a variety of situations,

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[99] See Review of Affiliate Transactions at Southwestern Bell Telephone Company, Joint Audit Report, at D-2 (May 1994).

[100] See id. at D-19.

[101] See id. at D-18 - D-19.

[102] See GTE Telephone Operating Companies, ADD 94-35, FCC 94-15, (released Apr. 8, 1994), at ¶¶ 1-2.

the most egregious were in relation to GTE's data processing services operations.[103] During this period, when GTE's regulated operations were permitted an authorized return on investment of 12 percent,[104] GTE's unregulated enhanced services generated a return on investment of between 22.1 and 25.5 percent on sales to GTE.[105] The enormous overcharge of GTE's regulated operations totaled $115.4 million, almost 10 percent of GTE's enhanced service revenues.[106]

What was the effect of such large cross-subsidization? During the period covered by the audit, at least one ITAA member was competing with GTE for a number of data processing contracts. GTE, however, won contract after contract. In every situation, GTE priced its services significantly below those of its competitors. Although the ITAA member in question concluded that GTE must have been pricing below its costs, it was unable to obtain proof. The ITAA company, moreover, concluded that even if it could develop the necessary evidence, no purpose would be served by filing a complaint with the Commission because the Commission could not re-award the lost contracts. Although the Commission's audit eventually exposed the cross-subsidies and GTE's ratepayers have been made whole, GTE's competitors have been damaged by the loss of these contracts and have no recourse from the audit. Even ratepayers had to wait up to six years after the subsidies took place before being made whole.

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[103] See GTE Telephone Operating Companies, AAD 94-36, FCC 94-16, (released Apr. 8, 1994), Summary passim.

[104] Id. ¶ 11.

[105] Id.

[106] Id.

Southern Bell Audit. The Georgia Public Service Commission ("PSC") conducted an extensive audit of Southern Bell's cost allocations for the years 1992 to 1994. The PSC concluded that Southern Bell had engaged in significant cross-subsidization of its unregulated activities, including its enhanced services.[107] The cross-subsidization was found to be widespread, ranging from voice messaging services to customer-premises equipment.[108] Although the PSC determined that Southern Bell was generally in compliance with the Commission's cost allocation rules,[109] the cross-subsidization nonetheless occurred. This audit, which took place subsequent to the supposed improvement in the Commission's accounting rules, demonstrates again that they are inadequate to prevent cross-subsidies.

MECO Audit. NYNEX established a separate unregulated, but less than fully separate, subsidiary -- NYNEX Materials Enterprise Company ("MECO") -- to purchase telecommunications equipment and other products and services and then to resell those products and services to the regulated NYNEX operating companies. Following press reports of anticompetitive activity, the Commission conducted an audit. The Commission's review disclosed that "MECO overcharged its regulated affiliates on sales of products and services, and that the regulated telephone companies, in turn, passed on the excessive costs

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[107] See Southern Bell Tel. & Tel. Co. Cost Allocations (Regulated/Nonregulated) and Affiliated Transactions, at I-1 - I-5 (Ga. PSC Sept. 1994).

[108] See id.

[109] See id. at I-4.

to the ratepayers."[110] The Commission's audit revealed that "MECO's total over-charges to its regulated affiliates from 1984 through 1988 were $118.50 million."[111] The Commission and NYNEX ultimately resolved the matter through a consent decree, seven years after the cross-subsidization in question began.[112] The fact that the Commission did not become aware of the cross-subsidization until after the press revealed the problem demonstrates just how ineffective the Commission's accounting and audit procedures are.

Inside Wiring. The Commission anticipated that, as a result of deregulation, the amount of inside wiring-related expenses that the BOCs allocated to their regulated accounts would decrease. When this did not occur, the agency investigated. The Commission's review revealed that the BOCs had misallocated more than $200 million in inside wiring costs from their non-regulated accounts to their regulated accounts.[113] The end result was that the BOCs' ratepayers were cross-subsidizing the carriers' provision of unregulated inside wiring, thereby providing the BOCs with an anticompetitive advantage in an adjacent market. Although the Commission uncovered these subsidies, it was after the fact and it did not undo the damage done to competitors.

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[110] New York Tel. Co. and New England Tel. Co.: Apparent Violations of the Commission's Rules and Policies Governing Transactions With Affiliates, 5 FCC Rcd 866, 868 (1990).

[111] Id. at 869.

[112] See New York Tel. Co. and New England Tel. & Tel. Co.: Apparent Violations of the Commission's Rules and Policies Governing Transactions With Affiliates, 5 FCC Rcd 5892 (1990), aff'd sub nom. New York State Department of Law v. FCC, 984 F.2d 1209 (D.C. Cir. 1993).

[113] The BOCs' conduct in the inside wiring market is discussed in the GAO Cross-Subsidization Report at 16.

GAO Reports. As described more completely above,[114] the GAO has twice conducted extensive studies of the Commission's ability to prevent cross-subsidization and has twice concluded that the Commission is not in a position to enforce its cost accounting and allocation rules.

2. **Access Discrimination.**

MemoryCall. One of the primary reasons underlying the Ninth Circuit's decision to vacate the Computer III Remand Order was the Commission's inability to explain BellSouth's anticompetitive behavior in the MemoryCall case, given the Commission's conclusions regarding the effectiveness of nonstructural safeguards.[115] In MemoryCall, the Georgia PSC found that BellSouth used its regulated operations' control over the local exchange to hamper competitors in the voice messaging market.[116] The PSC determined that BellSouth had used its control of switching equipment to ensure that competitors to MemoryCall could only offer service that was technically inferior to MemoryCall.[117] BellSouth also refused to allow competitors to collocate voice messaging equipment in BellSouth's central offices, which gave the competitors lower quality services and higher costs.[118] Finally, BellSouth "manipulated development of the local network, especially the timing of unbundling certain network features necessary for MemoryCall to be offered at all,

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[114] See supra pp. 38-41.

[115] See California III, 39 F.3d at 929.

[116] See MemoryCall Order, at 27-41.

[117] Id. at 28-30.

[118] Id. at 30-31.

in order to maximize its competitive advantage with respect to its initial offering of MemoryCall."[119] These anticompetitive actions caused serious harm to BellSouth's voice messaging competitors.[120]

None of the Commission's nonstructural safeguards prevented the anticompetitive abuse in MemoryCall. Because ONA was not fully implemented, competitors were denied access to unbundled network services. CEI, pursuant to which MemoryCall was offered,[121] also proved to be inadequate. Neither CEI nor ONA has changed much since 1991. The Expanded Interconnection orders would not provide any comfort in the context of the Memorycall dispute and the safeguard that would help -- physical collocation of enhanced services equipment -- is still not available to ESPs. These, as well as the Commission's other nonstructural safeguards, can therefore be expected to perform as poorly today as they did in 1991. Before the Commission can find nonstructural safeguards to be effective, it must address the abuses chronicled in the MemoryCall case.

Boston Phoenix. The Boston Phoenix, a New England newspaper, has a subsidiary that provides audiotext and voice messaging services for personal advertisements in over 300 newspapers, computer networks, and cable television systems, as well as on the Internet. These offerings depend on NYNEX-provided service for connection and billing purposes. Some time ago, the Boston Phoenix began discussions with NYNEX regarding the

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[119] Id. at 28.

[120] Additionally, the Public Service Commission ("PSC") suspected that BellSouth was cross-subsidizing MemoryCall service. Id. at 41-42. The PSC eventually performed an audit of Southern Bell which, as described above, found cross-subsidization of

possibility of including personal advertisements and their attendant audiotext and voice messaging services on NYNEX's proposed video dialtone systems. The discussions proceeded far enough that the Boston Phoenix created a prototype service and performed demonstrations for NYNEX. Having been apprised of the market for these enhanced services and their potential use in conjunction with video dialtone services, NYNEX broke off discussions with the Boston Phoenix. NYNEX then proceeded to require the Boston Phoenix to change its service from 976-service, to less desirable 940-service, in an apparent effort to impede the operations of a competitor. The Boston Phoenix obtained a preliminary injunction against NYNEX, largely on the basis that NYNEX was acting for competitive reasons to disadvantage the Boston Phoenix and create a market for its own enhanced services.[122]

ScanAlert. The actions of Ameritech in offering the ScanAlert alarm service also demonstrate how the BOCs are able to discriminate against competing ESPs.[123] ScanAlert is an alarm service technology that has functionality resident in Ameritech's wire and switching centers. Before Ameritech entered the alarm service business, Ameritech deployed ScanAlert technology. It then completely withdrew the technology to the detriment of ESPs that had developed services in reliance on ScanAlert. When Ameritech subsequently

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[122] Boston Phoenix, Inc. v. NYNEX Corp., No. 95-0059, slip op. at 6 (Mass. Dist. Ct. Feb. 3, 1995).

[123] For a complete analysis of ScanAlert, see Memorandum of Alarm Industry Communications Committee in Opposition to Ameritech's Motion for a Waiver to the Interexchange Restriction to Permit Acquisition of Alarm Monitoring Accounts Service Across LATA Boundaries, United States v. Western Elec. Co., Civ. No. 82-0192, (Feb. 15, 1995).

reentered the alarm services market, it reintroduced ScanAlert, but only in a fraction of its wire or serving centers.[124] In order for ESPs to obtain this previously available service, ESPs must now guarantee a certain volume of business.[125] Ameritech, of course, has the ability to deploy ScanAlert to benefit its own unregulated alarm service operations.

Telemessaging. The Association of Telemessaging Services International ("ATSI") has compiled reports of access discrimination by the BOCs against its member companies. Excerpts from that compilation have been placed in the record of this proceeding.[126] The reports demonstrate that the BOCs routinely violate the CPNI rules, "unhook" established customers of unaffiliated ESPs, provide poor quality connections and service, use services for their own unregulated activities that are denied to competing ESPs, and provide false information to consumers.[127] The large number of reports indicates that the abuse by the BOCs is widespread and not limited to one carrier. The large growth in the provisioning of enhanced services by the BOCs, cited approvingly by the Notice,[128] was aided by the anticompetitive activities chronicled by ATSI. They demonstrate that nonstructural safeguards have been unable to prevent access discrimination.

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[124] See id.

[125] See id.

[126] See Letter from Robert J. Butler to William F. Caton, CC Docket No. 95-20 (Dec. 13, 1994).

[127] Id. passim.

[128] See Notice ¶ 37. Of course, another significant reason for the increase in the number of BOC enhanced service customers between 1990 and 1994 is the lifting of certain information services restrictions by Judge Greene in 1991. See United States v. Western Elec. Co., 767 F. Supp. 308 (D.D.C. 1991), aff'd, 993 F.2d 1572 (D.C. Cir. 1992).

CPNI. Not content until the advantages they enjoy by virtue of the asymmetrical nature of the Commission's CPNI rules, the BOCs have also sought to use their control over the local exchange to obtain access to the CPNI of their larger customers. In July 1992, ITAA presented the Commission with evidence that BellSouth and Southwestern Bell had improperly pressured ITAA's member companies to gain access to their CPNI.[129]

In one incident involving BellSouth, an ITAA member company was told that its order for private line service would not be processed unless and until the company completed a CPNI "Response Form." The Response Form, however, presented ITAA's member company with only two choices; it could provide BellSouth with "access to all my CPNI" or it could provide BellSouth with "access to all my CPNI except specifically designated information." The Response Form did not provide ITAA's member with the option of denying BellSouth access to all of its CPNI.

In another incident involving Southwestern Bell, ITAA noted how the carrier's sales representatives had pressured an accounting clerk of an ITAA member company to sign a CPNI Authorization Form that did not provide the company with the option of denying Southwestern Bell access to its CPNI. Moreover, the Form -- even though signed by an accounting clerk in a small office of a national company -- would have provided the carrier with access to the CPNI of "all subsidiaries, locations and accounts associated with my company." ITAA also reported that the two carriers had advised yet another ITAA member

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[129] See Letter from Joseph P. Markoski to Alfred C. Sikes (July 8, 1992).

company that the Commission's rules permit them to deny basic service to customers that refuse to provide the BOCs with access to their CPNI.

Other Abuses. In addition to the more well-publicized instances of abuse, there are countless other examples of anticompetitive conduct which have not been, and never will be, reported. When an ESP or an ESP's customer encounters difficulty in obtaining timely or quality service from a BOC, the problem usually generates a great deal of discussion between the BOC and the ESP or the ESP's customer. If a BOC is being particularly difficult, the problem may generate a call to the local public utility commission ("PUC"). Usually, these calls involve an inquiry about the user's right to demand quality or timely service from the BOC and, occasionally, they may produce a call to the carrier by a member of the PUC's staff. These inquiries and follow-up calls are rarely, if ever, memorialized in any official report or record.

They also rarely result in the filing of a formal or informal complaint. The reasons for this are relatively obvious. Once a problem has been solved -- e.g., a line has been installed or its quality improved -- no purpose is served by filing a complaint. The customer has already achieved its goal. Moreover, because the relationship between a carrier and its customer is ongoing, many business people are reluctant to sour the relationship even further by filing a complaint once a problem has been satisfactorily resolved. In addition, most people recognize that even a successfully prosecuted complaint cannot undo the competitive damage caused by a BOC's cross-subsidies or access discrimination. A PUC cannot recover a lost customer or award an injured ESP lost revenues.

Further, there is the difficulty, delay and attendant expense in proving cross-subsidization and access discrimination, particularly against a BOC with enormously deep pockets and a regulatory staff already on board. Indeed, the resources required to pursue a complaint oftentimes outweigh any conceivable recovery. Given all these factors, it should not be surprising that ITAA's member companies did not pursue a complaint against GTE when it suspected -- and the Commission ultimately found -- that the carrier was cross-subsidizing its unregulated enhanced service operations.[130]

C. Structural Separation Has Lower Costs Than Nonstructural Safeguards.

As set forth above, nonstructural safeguards are less than effective in preventing anticompetitive cross-subsidization and access discrimination. The Commission has never been able to persuade the Ninth Circuit otherwise. Nonstructural safeguards, however, also have another major disadvantage. They impose enormous administrative costs on the Commission, the carriers and the public at large.

Because nonstructural safeguards are, in essence, an effort to replicate the effectiveness of structural safeguards through a series of behavioral and reporting requirements, they are inherently more complex. Thus, the Commission has been required to devote a great deal of time in the first instance to developing accounting, auditing, CEI, ONA, CPNI, and nondiscrimination reporting rules.[131] Once adopted, these rules have

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[130] See supra note 103 and accompanying text.

[131] This has already consumed and, in ITAA's view, wasted millions of dollars. ONA is a classic example of a nonstructural safeguard to which the Commission, the carriers (continued...)

required the Commission to devote scarce resources -- which could more profitably be used elsewhere -- auditing the BOCs' integrated operations, evaluating service-specific CEI plans, reviewing the BOCs' nondiscrimination and ONA reports, investigating the carriers' ONA tariffs, and otherwise attempting to ensure that the BOCs comply with the Commission's nonstructural safeguards.

Given their limited utility in preventing anticompetitive abuse, the Commission's nonstructural safeguards have become a paper chase in both form and substance. One need only glance at the mountains of paper which the BOCs must file with the Commission in accordance with its nonstructural safeguards to appreciate this point. The Commission's rules themselves illustrate this problem. Whereas the Commission's structural separation and transactions between affiliates rules can be found in two sections covering two pages of the Code of Federal Regulations,[132] its nonstructural safeguards require an analysis of rules and orders covering literally hundreds of pages.[133]

Structural separation, by contrast, imposes relatively few burdens on the Commission. Once the Commission has approved the initial formation of the BOCs'

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[131](...continued)
and others have devoted enormous resources without gaining any tangible benefits in return.

[132] See 47 C.F.R. §§ 32.27 & 64.702 (1994).

[133] E.g., id. §§ 32.23, 32.1406, 64.901-04 & 69. Other nonstructural safeguards have requirements that have not been codified, including CEI, ONA and network disclosure requirements.

subsidiaries, the templates for which already exist,[134] the Commission need only act as a "border guard," monitoring transactions between regulated parent and unregulated affiliate. (Although ITAA does not wish to minimize the importance or burden of this undertaking, monitoring transactions between affiliates is substantially less burdensome than reviewing millions of daily transactions between a carrier's regulated and unregulated integrated operations.)[135] Equally important, structural separation -- unlike nonstructural safeguards -- minimizes the need for the Commission to monitor the business of, require reports from, and otherwise become involved with, the carriers' unregulated operations.

Just as nonstructural safeguards impose burdens on the Commission, they also impose costs on the carriers. The Commission's complex web of nonstructural safeguards requires the carriers to divert resources to regulatory compliance that could otherwise be productively used to provide enhanced services. Again, the mountains of paper which the BOCs routinely file with the Commission are testament to this fact. A prime example of the

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[134] The BOCs, at one time, all had Computer II subsidiaries through which they offered enhanced services. The Commission has already addressed the formation of these subsidiaries. See BOC Separation Order, 95 F.C.C.2d at 1138-19; American Information Technologies, Inc., 102 F.C.C.2d 1089 (1985); American Tel. & Tel. Co., 90 F.C.C.2d 404 (1982).

[135] Indeed, the Commission has found that:

> [s]tructural separation reduces the common transactions between providers of basic services and affiliated providers of competitive offerings, and highlights transactions such as the flow of funds, transfers of information, and the procedures for accomplishing interconnection by affiliated vendors.

Policy and Rules Concerning the Furnishing of Customer Premises Equipment, Enhanced Services and Cellular Services by the Bell Operating Companies, FCC 84-252, at ¶ 15.

wasted effort required by the Commission's nonstructural safeguards is the investigation of the BOCs' ONA tariffs.

As noted above, ONA is not being used by independent ESPs. Rather, the primary customers of the BOCs' ONA offerings are IXCs that were -- over their strenuous objection -- required to forego Feature Group Service and purchase BSAs and BSEs instead (in order to obtain equivalent service). Notwithstanding the obvious irrelevance of ONA as a competitive safeguard for enhanced services, the carriers -- both BOCs and IXCs -- engaged in a protracted struggle over these tariffs for many years. Indeed, the dispute over U S West's tariff still remains pending.[136] ITAA cannot conceive of a justification for such wasted effort.

The costs of structural separation, by contrast, are largely one-time expenses for the BOCs. Once a separate subsidiary has been established, the day-to-day costs of a structurally separated, as opposed to integrated, enhanced service operation are essentially non-existent. The BOCs have never proven otherwise. Indeed, they cannot. Unless a BOC has excess idle personnel, facilities and computers (which, according to the BOCs, they do not), a BOC would have to acquire all of these things in order to start a new enhanced services business.

Even the one-time costs of establishing a separate subsidiary are overstated. Several of the BOCs already appear to conduct some or all of their enhanced service operations through separate -- albeit not Computer II -- subsidiaries. Further, it appears that

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[136] See Open Network Architecture Tariffs of U S West Communications, Inc., 9 FCC Rcd 6710 (1994).

Congress is likely to require the BOCs to provide some subset of information services, manufacturing and interexchange services through fully separate subsidiaries.[137] The incremental cost, if any, of requiring the BOCs to provide enhanced services through these subsidiaries will plainly be lower than requiring an entirely new subsidiary. Moreover, to the extent that creating a separate subsidiary can be shown to be a burden, the Commission can always provide the BOCs with a suitable amount of time to establish these subsidiaries.

Finally, and perhaps most importantly, there are the costs which nonstructural safeguards impose on consumers. Nonstructural safeguards, because of their ineffectiveness in preventing cross-subsidization and access discrimination, burden ratepayers with inflated rates for basic regulated services. Consumers also suffer when the BOCs' access discrimination limits the availability of competing enhanced services. The economy as a whole also suffers when anticompetitive cross-subsidization and access discrimination create artificial market conditions and cause the BOCs, their competitors and consumers to allocate resources in ways in which they otherwise would not.

Structural separation, on the other hand, helps ensure a truly competitive environment and, in doing so, allows marketplace forces to dictate the efficient allocation of resources and to influence consumer choice. A competitive marketplace also drives prices towards cost and inefficient producers (as opposed to the victims of cross-subsidization or discrimination) out of the market. Consumers only stand to benefit from such an environment.

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[137] See, e.g., S. 625, 104th Cong., 1st Sess. (1995); S. 1822, 103d Cong., 2d Sess. (1994); H.R. 3626, 103d Cong., 2d Sess. (1994).

V. THE BENEFITS OF THE INTEGRATED PROVISIONING OF ENHANCED SERVICES BY THE BOCS ARE MINIMAL.

As set forth above, structural separation is far more effective than nonstructural safeguards in preventing anticompetitive cross-subsidization and access discrimination. As also set forth above, structural separation imposes fewer costs on the Commission, the carriers and the public than nonstructural safeguards. Given these facts, the question which immediately presents itself is why the Commission is giving any serious thought to nonstructural safeguards. ITAA surmises that it is the oft-repeated, but never documented, notion that there are benefits to allowing the BOCs to integrate their basic and enhanced service operations that are not available to independent enhanced service providers.

The reality, however, is that there are few, if any, real benefits to such integration. There is no better proof of this fact than today's enhanced services marketplace. The United States is now, and always has been, the acknowledged world leader in the provision of enhanced services. No other country even comes close to approaching the number, sophistication or variety of enhanced services that are available to consumers in the United States.

Significantly, none of the major U.S. providers of enhanced services is a carrier with integrated basic and enhanced service operations. Rather, out of the many thousands of enhanced service providers, all but a few are "structurally separated" from the basic communications network. In other words, the United States has achieved its preeminent position in the global information services marketplace without the alleged

"benefits" of integrating the provision of basic and enhanced services.[138] By contrast, many of the countries which have lagged behind in information services are those which pursued the integrated provision of basic and enhanced services. As these countries have focused on the need to improve the quality, variety and number of enhanced services available to their citizenry, they have looked to the separation, rather than the further integration, of basic and enhanced services.

Certainly, there are no technological advantages to the integrated provision of basic and enhanced services. As the Commission has previously recognized, the intelligence in intelligent networks is moving out of the central office and into remote databases.[139] This means that enhanced services can be provided more efficiently "outside" of the network than as an integral part of it, contrary to what the Commission appeared to assume ten years ago when it began Computer III.[140] Significantly, the BOCs did not seriously argue otherwise in Computer III. And, to the extent that new and innovative enhanced services can

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[138] An independent ESP has a marketplace incentive to provide its services in the most efficient and technologically advanced manner possible, whether it be through hardware, software or network services. An independent ESP also has an economic incentive to make the most efficient use, and thereby reduce the cost, of the communications services upon which it relies to deliver its enhanced services to its customers. A carrier with integrated enhanced service operations does not have the same incentives. Rather, because it has an economic interest in the use of its network, a BOC is more likely to look to network-based solutions to provide enhanced services, even if they are not the most economically or technologically efficient.

[139] See Intelligent Networks, Notice of Inquiry, 6 FCC Rcd 7256, 7257 (1991).

[140] Computer III Phase I Order, 104 F.C.C.2d at 1007.

only be provided on an integrated basis, the Computer II waiver process has proven to be effective in dealing with such instances.[141]

Integration also most certainly does not produce innovation. Because of MFJ restrictions, the only enhanced services being offered by the BOCs are provided entirely over their own facilities. If integration produced technological innovation, the BOCs should be market leaders. As the marketplace can attest, however, the BOCs' integration has not produced any innovative or new enhanced services. Indeed, the only enhanced services market in which the BOCs have achieved any measurable success is the voice messaging market where, as noted above, their success has been achieved through access discrimination and cross-subsidization.[142]

In Computer III, the BOCs made an eleventh-hour attempt to demonstrate the costs and benefits of integrating their basic and enhanced service operations. The only significant "benefit" that the BOCs were able to identify is their ability to use their existing relationships with business and residential consumers to market their voice messaging services. In making these claims, the BOCs emphasized the difficulties they would encounter if they were compelled to engage in "cold calling," rather than capture incoming calls to their telephone company business offices, for enhanced service sales.[143] The problems they identified, however, are precisely those faced by independent ESPs. The "benefit" of such

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[141] See Petitions for Waiver of Section 64.702 of the Commission's Rules (Computer II), 100 F.C.C.2d 1057 (1985).

[142] See MemoryCall discussion supra pp. 48-49.

[143] See, e.g., Letter from Trudi W. Blair, Bell Atlantic to Donna Searcy, CC Docket No. 90-623 (Nov. 7, 1991).

privileged access to consumers is more than offset by the competitive harm which such access has already caused in the voice messaging industry.

ITAA does not know what new arguments the BOCs will advance about the "benefits" of integration in their initial comments in this proceeding. ITAA, however, submits that the following observations, which were part of the record in Computer III, will apply:

> Cutting through the rhetoric about efficiency and customer convenience, the essence of the RBOCs' vision of integrated basic/enhanced operations lies in their ability to gain maximum marketing advantage, to use existing captive relationships with customers of basic monopoly services as leverage points for promoting and for selling nominally competitive enhanced services. Similar claims could readily be advanced by virtually any monopoly in virtually any industry; indeed, if an efficiency defense were permitted, most antitrust laws and principles would lose all meaning. Clearly, and concededly, there are small efficiency gains that may arise when a small start-up activity is integrated into a large, well-established business with a large, well-established customer base. But the essence of the FCC's competitive policies over the past two decades has been to forego small, short-run efficiencies in favor of a more robust competitive marketplace over the long haul. The RBOC filings confirm that the only tangible result of integrated operation is to introduce formidable barriers to competition; the public detriment of such barriers far exceeds the nominal private efficiency gains that would flow to the RBOCs' owners.[144]

The burden is therefore on the BOCs to demonstrate: (1) that there are cognizable public interest benefits arising from their integrated provision of basic and enhanced services; (2) that these public benefits outweigh the effectiveness of structural separation in preventing cross-subsidization and access discrimination; and (3) that these

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[144] Lee R. Selwyn, "The Costs of Separate Subsidiaries," at 7-8 (accompanying Letter from James S. Blaszak to Donna R. Searcy (Nov. 12, 1991)) (emphasis in original).

public benefits outweigh the sizable costs which nonstructural safeguards impose on the Commission, the carriers and the public. Absent such a showing, the Commission should affirm the continuing applicability of the structural separation requirements of Computer II.

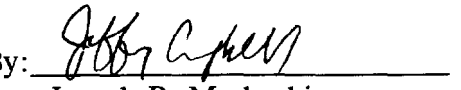
VI. CONCLUSION

As set forth above, a necessary consequence of the Ninth Circuit's decision in California III is to require the Commission either to accept Computer II or to undertake an entirely new analysis of the costs and benefits of structural and nonstructural safeguards. Upon conducting such an analysis, the Commission can only conclude that the benefits of structural separation in preventing anticompetitive abuse and minimizing the burdens on the Commission far outweigh the one-time costs of establishing separate subsidiaries. Nonstructural safeguards, by contrast, produce no benefits and impose continuing costs of compliance on the carriers and oversight burdens on the Commission. Combined with the increased risks of anticompetitive abuse which attend nonstructural safeguards, these costs far outweigh any perceived public benefits of integrating the BOCs' monopoly local exchange and competitive enhanced service operations. The Commission should therefore affirm the

continued vitality of Computer II and require the BOCs to provide enhanced services through fully separate subsidiaries pursuant to Section 64.702 of its rules.

Respectfully submitted,

INFORMATION TECHNOLOGY
ASSOCIATION OF AMERICA

By: 

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